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U.S. Insurer Total Exposure to Schedule BA (Other Long-Term Invested Assets) Rises 10% at Year-End 2019

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Executive Summary

- U.S. insurer exposure to Other Long-Term Invested Assets (as reported in Schedule BA) increased by 10% to \$401.8 billion in book/adjusted carrying value (BACV) at year-end 2019 from \$365.2 billion at year-end 2018 (including affiliated and unaffiliated investments).
- Total unaffiliated exposure was \$162.3 billion at year-end 2019, up from \$160.6 billion at year-end 2018.
- Private equity (PE), hedge funds (HF) and real estate (RE) have continued to represent the three largest asset types within U.S. insurers' total Other Long-Term Invested Assets, totaling \$297.6 billion.
 - Unaffiliated PE, HF and RE increased by 9% in aggregate to \$82.2 billion, \$25.5 billion and \$16.1 billion, respectively, or \$123.9 billion in total.
 - About 36% of U.S. insurers had exposure to unaffiliated PE, HF and RE that exceeded 10% of total capital and surplus, which was consistent with year-end 2018.
- Mortgage Loans were 7% of total Other Long-Term Invested Assets, but they increased almost three-fold, to about \$27 billion at year-end 2019 from approximately \$10 billion at year-end 2018 (or 3% of total Other Long-Term Invested Assets).

Other Long-Term Invested Assets – The Majority Continues to Comprise PE, HF and RE

A significant proportion of U.S. insurers' investments reported in Schedule BA, or Other Long-Term Invested Assets, have been in joint ventures (JV), partnerships, and limited liability companies (LLCs) that have the underlying characteristics of common stock (primarily PE funds), RE (primarily RE funds, not including mortgages) or "other" (primarily HF). Schedule BA investments have also historically included a relatively even split between affiliated and unaffiliated investments (at least over the last few years).

Total U.S. insurer exposure to Other Long-Term Invested Assets was \$401.8 billion in BACV at year-end 2019, an increase of 10% from \$365.2 billion at year-end 2018 (see Table 1 and Table 2). They were also almost 6% of U.S. insurers' total cash and invested assets, similar to year-end 2018. Affiliated Other Long-Term Invested Assets accounted for \$239.5 billion, or 60% of the total, with the remaining 40% in unaffiliated investments, or \$162.2 billion, at year-end 2019.

PE, HF and RE, totaling \$297.6 billion (74% of total Other Long-Term Invested Assets), were the largest three asset types, consistent with prior years. In comparison, at year-end 2018, PE, HF and RE totaled \$272.5 billion and were also 74% of total Other Long-Term Invested Assets.

Table 1: U.S. Insurer Schedule BA Exposure as of Year-End 2019 (BACV, \$Mil.)*

Asset Type	Life*	P/C	Title	Health	Total	% of Total
Other - JV (Hedge Fund, HF)	31,931	84,610	121	5,081	121,743	30%
Common Stock - JV (Private Equity, PE)	92,553	20,297	-	4,204	117,053	29%
Real Estate - JV (RE)	39,636	17,968	1	1,252	58,857	15%
Mortgage Loans - JV (Mortgage Loans)	20,944	5,725	15	497	27,181	7%
Any Other Class of Assets/Other	6,387	15,701	20	1,413	23,521	6%
Surplus Debentures	15,034	2,637	8	424	18,103	5%
Collateral Loans	9,223	1,470	-	375	11,068	3%
Non-collateral Loans	180	13,120	-	315	13,616	3%
Non-Guaranteed Federal Low Income Housing Tax Credit	4,534	2,805.33	-	114.26	7,454	2%
Capital Notes	3,060	-	-	167	3,227	1%
Total	223,483	164,334	165	13,842	401,823	100%
% of Total	56%	41%	0%	3%	100%	

*As of year-end 2019, fraternal companies' exposures are included with life companies' exposures due to a reporting change.

Table 2: U.S. Insurer Schedule BA Exposure as of Year-End 2018 (BACV, \$Mil.)

Asset Type	Life	P/C	Fraternal	Title	Health	Total	% of Total
Other - JV (Hedge Fund, HF)	24,429	81,875	708	106	5,324	112,442	31%
Common Stock - JV (Private Equity, PE)	80,142	17,534	3,916	1	3,786	105,379	29%
Real Estate - JV (RE)	35,321	17,772	468	1	1,182	54,744	15%
Mortgage Loans - JV (Mortgage Loans)	8,898	304	322	38	108	9,669	3%
Any Other Class of Assets/Other	15,370	16,875	37	18	1,661	33,961	9%
Surplus Debentures	13,155	2,625	207	3	402	16,392	4%
Collateral Loans	7,501	1,498	3	0	179	9,181	3%
Non-collateral Loans	71	13,084	6	4	338	13,503	4%
Non-Guaranteed Federal Low Income Housing Tax Credit	4,720	1,900	-	-	85	6,704	2%
Capital Notes	199	2,831	-	-	166	3,196	1%
Total	189,806	156,298	5,667	171	13,229	365,172	100%
% of Total	52%	43%	2%	0%	4%	100%	

Life companies accounted for the majority of U.S. insurers' Other Long-Term Invested Assets at about 56% of the total at year-end 2019. The proportion of PE, HF and RE was relatively consistent year-over-year (YOY), but Mortgage Loans JV increased almost three-fold to \$27.1 billion at year-end 2019 from \$9.6 billion at year-end 2018, perhaps due to attractive yields for mortgages relative to other lower yielding fixed-income securities. Note that about 6% of U.S. insurers' Mortgage Loan JV exposure at year-end 2019, or \$1.5 billion, was unaffiliated; i.e., \$25.6 billion was affiliated.

Unaffiliated – HF, PE and RE

Approximately 40% of U.S. insurers' Other Long-Term Invested Assets were unaffiliated and totaled \$162.3 billion at year-end 2019, compared to 43% at year-end 2018, or \$160.6 billion. New York-domiciled insurers accounted for the largest state exposure at 22% of the U.S. insurance industry's total unaffiliated Other Long-Term Invested Assets at year-end 2019.

The combined U.S. insurer exposure to unaffiliated PE, HF and RE investments increased by an aggregate 8% to \$82.2 billion, \$25.5 billion and \$16.2 billion, respectively, from \$73.9 billion, \$25 billion and \$15.5 billion, respectively, at year-end 2018 (see Table 3 and Table 4).

Table 3: U.S. Insurer Exposure to Unaffiliated HF, PE and RE as of Year-End 2019 (BACV, \$Mil.) *

Asset Type	Life*	P/C	Health	Title	Total	% of Total
PE	62,407	18,644	1,176	-	82,227	66%
HF	9,501	13,056	2,964	9	25,530	21%
RE	9,192	5,818	1,189	1	16,199	13%
Total	81,100	37,518	5,328	10	123,956	100%
% of Total	65%	30%	4%	0%		

* As of year-end 2019, fraternal companies' exposures are included with life companies' exposures.

Table 4: U.S. Insurer Exposure to Unaffiliated HF, PE and RE as of Year-End 2018 (BACV, \$Mil.)

Asset Type	Life	P/C	Fraternal	Health	Title	Total	% of Total
PE	55,511	16,746	472	1,130	-	73,860	65%
HF	7,336	14,409	538	2,820	8	25,110	22%
RE	7,250	6,683	383	1,136	1	15,453	14%
Total	70,097	37,838	1,393	5,087	8	114,423	100%
% of Total	61%	33%	1%	4%	0%	100%	

Life and property/casualty (P/C) companies together accounted for an aggregate of \$118.6 billion at year-end 2019, or 96% of total unaffiliated PE, HF and RE, compared to about \$108 billion at year-end 2018, or 94% of total unaffiliated PE, HF and RE.

Unaffiliated Other Long-Term Invested Assets by Assets Under Management (AUM)

Consistent with year-end 2018, large insurers (those with total cash and invested asset greater than \$10 billion) accounted for the majority (76%) of exposure to unaffiliated Other Long-Term Invested Assets as of year-end 2019 (see Table 5).

Table 5: U.S. Insurer Exposure to Unaffiliated Other Long-Term Invested Assets by Total Cash and Invested Assets as of Year-End 2019 (BACV, \$Mil.)

Asset Type	Between							Grand Total
	Less Than \$250MM	Between \$250MM and \$500MM	\$500MM and \$1.0B	Between \$1.0B and \$2.5B	Between \$2.5B and \$5.0B	Between \$5.0B and \$10.0B	Greater Than \$10B	
HF	173	532	1,145	3,302	2,463	2,325	15,591	25,530
PE	202	282	599	2,600	1,938	6,542	70,065	82,227
RE	101	49	382	1,185	545	2,695	11,242	16,199
Other BA assets	585	381	827	2,914	3,123	3,657	26,828	38,314
Total	1,060	1,243	2,953	10,001	8,068	15,219	123,726	162,270
% of Total	1%	1%	2%	6%	5%	9%	76%	100%

Total Capital and Surplus

When U.S. insurers' exposure to an asset type exceeds 10% of total capital and surplus, there is a potential for liquidity risk. In particular, investments reported in Schedule BA may be considered "alternative investments" — i.e., not conventional and often higher-yielding than traditional assets due in part to their complexity — so concerns regarding liquidity risk with these investments may be heightened compared to the more traditional asset types, such as municipal or corporate bonds. At year-end 2019, about 36% of U.S. insurers with unaffiliated exposure (363 in number) reported that it was more than 10% of total capital and surplus. This trend was consistent with year-end 2018.

PE, HF and RE Market Updates

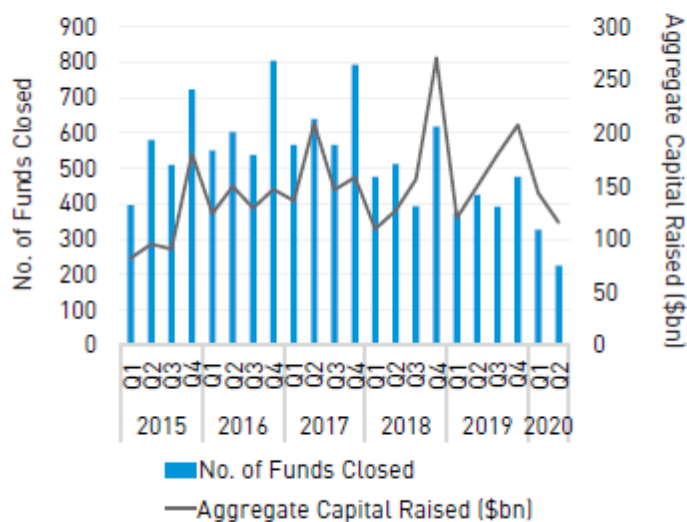
With the widespread impact of the COVID-19 pandemic on the global economy, some PE, HF and RE have experienced a decrease in AUM, capital raising, and/or returns since year-end 2019. While the largest components of Other Long-Term Invested Assets at year-end 2019 comprised U.S. insurer investments to unaffiliated PE, HF and RE, they were a small portion of overall U. S. insurer investments (approximately 2% of total cash and invested assets), mitigating concern. Also lending comfort, for PE, the number of funds in the market has increased from January through July 2020 (despite a decrease in targeted capital); HF achieved noteworthy gains in Q2 2020; and RE experienced an increase in capital raised. However, for U.S. insurers where concentrations of PE, HF and/or RE are high relative to total capital and surplus, a review of this exposure may be warranted.

PE

PE fundraising in 2019 totaled about \$600 billion in 1,316 funds according to Preqin, a provider of alternative assets data, due in part to a strong deal market and positive investor sentiment (see Chart 1).¹ In addition, dry powder for PE, or the amount of committed but unallocated capital, reached a record high \$1.43 trillion as of December 2019. Due in part to COVID-19-related lockdowns, \$116 billion in aggregate capital was raised in Q2 2020 across 225 funds, the lowest amount since \$110 billion in Q1 2018.² PE AUM totaled more than \$4.5 trillion as of December 2019.

Chart 1: Global Quarterly PE Fundraising

Fig. 1: Global Quarterly Private Equity Fundraising, Q1 2015 - Q2 2020



Source: Preqin Pro

The annualized net internal rate of return (IRR) for all PE was just under 20% YOY as of December 2019; buyout strategies had the highest annualized YOY IRR at 20.5%. In 2019, PE-backed buyout deals seeking capital were

¹ Preqin, *2019 Private Equity Venture Capital Update Factsheet*, January 2020.

² Preqin, *Preqin Quarterly Update: Private Equity & Venture Capital Q2 2020*, July 2020.

valued at \$393 billion, down from \$493 billion in 2018. Overall, PE funds were seeking to raise \$884 billion in capital as of July 2020, down from \$926 billion in January due in part to the economic impact of COVID-19.

HF

According to BarclayHedge, a source of alternative investment data, HF AUM decreased to \$2.9 trillion as of Q1 2020, due in part to a decline in launch activity, down from \$3.2 trillion at Q4 2019. This is the first time HF AUM have been below \$3 trillion since Q3 2016, after reaching a peak of about \$3.3 trillion in Q4 2019. Total net outflows in Q1 2020 were \$366.5 billion, due mostly to performance losses, and it represented the fourth highest net outflows in HF history.³ HF returns were 11.48% in Q2 2020 according to Preqin—the largest quarterly return since Q2 2009 (14.62%)—as global lockdowns related to COVID-19 eased, resulting in an increase in consumer spending and stock market valuations, with HF that represented equity strategies contributing a 14.65% gain in Q2 2020.⁴ Nevertheless, HF returns for Q1 2020 were still below zero at -0.37%; and Q2 gains, while meaningful, were not sufficient to eradicate the -10.63% losses that occurred in Q1 2020.

RE

The number of RE funds that closed in Q2 2020 decreased to 53, according to Preqin, from 78 in Q1 2020, but total capital raised increased to \$39 billion from \$28 billion for the same time period.⁵ The total number of RE funds was 903 in July; North America accounted for the largest geographic region at 45% of all funds closing in Q1 2020, followed by 32% in Europe. While RE investors are moving into higher risk strategies, according to Preqin, they are also focused on low-risk managers, particularly during the current economic uncertainty related to COVID-19. There was a record \$3.6 trillion in RE AUM globally at year-end 2019, based on a survey conducted by three RE associations located in North America, Europe and Asia.

Summary

About 1,000 U.S. insurers reported exposure to Other Long-Term Invested Assets with a BACV of about \$401 billion, including affiliated and unaffiliated exposure, an increase of 10% from \$365.2 billion at year-end 2018. Unaffiliated Other Long-Term Invested Assets exposure increased to \$162.3 billion at year-end 2019 from \$160.6 billion at year-end 2018. Similar to prior years, PE, HF and RE were the largest asset types within Other Long-Term Invested Assets at year-end 2019; unaffiliated PE, HF and RE totaled approximately \$124 billion at year-end 2019, an increase of 9% over 2018, with PE being the largest at \$82.2 billion compared to \$73.9 billion at year-end 2018.

For the U.S. insurance industry, unaffiliated Other Long-Term Invested Assets represented 12% of total capital and surplus, but only 2% of total cash and invested assets, as of year-end 2019. For most U.S. insurers (64%), exposure to Other Long-Term Invested Assets represented 10% or less of total capital and surplus. For insurers where exposure to Other Long-Term Invested Assets exceeded 10% of total capital and surplus, which totaled about 360 in number, liquidity may be a concern.

The Capital Markets Bureau will continue to monitor trends in U.S. insurers' Other Long-Term Invested Assets and report on any developments as deemed appropriate.

³ Pension & Investments, *Hedge Fund Industry AUM Slips Below \$3 Trillion*, April 2020.

⁴ Preqin, *Preqin Quarterly Update: Hedge Funds, Q2 2020*, July 2020.

⁵ Preqin, *Preqin Quarterly Update: Real Estate, Q2 2020*, July 2020.

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